



Title: **Steering Group**

Paper: Fair funding review of relative needs and resources: discussion paper on relative resources - council tax and sales, fees and charges by the Ministry of Housing, Communities and Local Government

Date: 23 July 2018

Venue: Local Government Association, 18 Smith Square, London

POLICY DEVELOPMENT: NOT A STATEMENT OF GOVERNMENT POLICY

Introduction

1. On implementation of the Fair Funding Review, a local authority's share of the quantum available for redistribution at Local Government Finance Settlements (LGFS) will depend on an assessment of:
 - a. its relative funding need to deliver public services;
 - b. as well as its local revenue raising capacity to meet these costs - or relative resources;
 - c. any requirement for fixed-term transitional adjustments.
2. There are different options for making an assessment of relative needs and resources as part of a LGFS methodology, which will account for each to varying degrees.
3. Much of the focus to date, as reflected in the December 2017 consultation, was on relative needs, and estimating a local authority's 'need to spend' on public services through the examination of key cost drivers like population, deprivation, rurality etc.
4. This paper focuses on relative resources, specifically council tax and sales, fees and charges. There has also been progress in this work stream, and the Fair Funding Review Technical Working Group (FFR TWG) has received the following papers on relative resources and council tax:

- **August 2016:** Paul Woods, North East Combined Authority – differences in ability to raise council tax income
 - **January 2017:** MHCLG – approach to relative resources (introductory)
 - **July 2017:** MHCLG – a more detailed scoping paper on factors which affect council tax income, which need to be accounted for, including those easily influenced by authorities and those not; as well as on sales, fees and charges
 - **July 2017:** Paul Woods - Local Council Tax Support
 - **July 2017:** Society of County Treasurers – Council tax ‘the picture in numbers’ and response to MHCLG paper
 - **November 2017:** SIGOMA – on how the resources adjustment operated under the Four Block Model; the current RSG methodology; LCTS; the ASC precept
 - **November 2017:** MHCLG – different methodologies of accounting for council tax income in funding distributions based on recent precedents; as well as a scoping paper on Local Council Tax Support
 - **May 2018:** MHCLG – to establish a precise definition of the tax base for measuring relative resources, and seek views on whether particular factors which affect council tax income should be looked at more closely
5. The review will need to determine a measure of council tax income, such that authorities with a greater sum of that measure receive relatively larger downward adjustments to their needs share.
 6. Local authorities raise varying amounts of council tax income due to differing sizes of tax bases, as well as differing council tax levels set each year, subject to collection rates.
 7. The review will also need to agree a treatment of other local income including sales, fees and charges. This paper summarises some of the key issues, as well as key points which have been discussed and some the conclusions reached by the TWG for the views of the Steering Group.

Council tax elements

8. In designing a new resources block and measure of council tax income, the review will need to determine a treatment of all elements of council tax income, including both the tax base and tax levels.

Council tax base

9. The FFR must agree a comprehensive list of factors which affect the council tax base to establish a measure of local authorities’ resources. The tax base is relatively uncontroversial, with exceptions.

10. The tax base is defined as the number of Band D equivalents after discounts, exemptions and premiums. Some of these discounts, exemptions and premiums are set nationally, whilst others are set at local discretion. Methodologies in previous LGF Settlements have imposed assumptions on those set with local discretion, in part so that local decisions do not affect future funding allocations. Examples include the second homes and empty homes discounts.
11. Since the previous methodology (the 4-Block Model) last calculated relative needs and resources, there have been changes in policy which mean some council tax discounts and premiums exist with no precedent in the current methodology – most significantly Local Council Tax Support (LCTS).
12. At an England level, the effect on the national council tax base of most discounts and exemptions can be considered small, perhaps with the exception of the Single Person Discount (which equates to around 7% of the pre-reductions taxbase) and LCTS (which equates to around 10%). The next largest effect is that of all classes of exemption, which total 2%. Nonetheless, at a local authority level the effect of a given discount or exemption varies – the impact of council tax exemptions can range between around 1 – 15%.

Discounts, exemptions and premiums at England level

	Date introduced	Mandatory / Discretionary	Band D equivalent dwellings	Resulting percentage change in base
Dwellings on valuation list (initial)	n/a	n/a	22,236,414	n/a
Exemptions	n/a	Mandatory	-488,790	-2.2%
Demolitions	n/a	Mandatory	-1,312	0.0%
Disabled reduction	1993	Mandatory	-128,130	-0.6%
Disabled relief	1993	Mandatory	109,653	0.5%
Single Person discount	1993	Mandatory	-1,619,440	-7.3%
25% discounts	1993	Mandatory	-48,969	-0.2%
50% discounts	1993	Mandatory	-20,580	-0.1%
Second Homes discount		Discretionary	-2,647	0.0%
Empty Home discount		Discretionary	-45,317	-0.2%
Empty Home premium		Discretionary	25,518	0.1%

Family Annex discount	2014	Discretionary	-2,092	0.0%
Class O (military) exemptions	1993	Mandatory	-38,386	-0.2%
Reduction due to Local Council Tax Support	2013	Discretionary	-2,155,143	-9.7%
Final Taxbase			17,897,658	

13. In discussion over the last year, including in response to a March 2018 paper by MHCLG¹, the TWG came to a consensus that the review should continue to include all non-discretionary discounts and exemptions in its measure of tax base for the purpose of a resources adjustment, recognising that areas with relatively more such residents eligible will receive a smaller downward adjustment to its needs share (i.e. more funding allocated).

14. There was also a consensus that the review should continue an assumptions-based approach to discretionary discounts and exemptions, to avoid local authority policy directly affecting their settlement income (for example by granting more of a discount purposely to receive a higher allocation of funding at LGF Settlements).

Q. Does the Steering Group agree with the direction set out above for how to approach the tax base in respect of a relative resources adjustment?

15. The TWG has held separate discussions on LCTS, for which there is no precedent, and which stands out due to its size and origin as a needs allocation 'rolled-in' to the LGFS in 2013-14. Due to the discretionary nature of the working-age element of this discount, reflecting it in such a way that actual proportional measures of income forgone as recorded in Council Tax Base (similar to non-discretionary discounts) could lead to 'perverse incentives' and so has not been supported.

16. One alternative possible approach mentioned would be to find an objective measure of the number of potential claimants of support in a local authority, multiplied by the cost of a standard relief scheme, and reflected in the resources adjustment. The feasibility of such an approach is yet to be tested.

17. Several members pointed out that the pensioner element is non-discretionary, meaning this element of income forgone (as captured by Council Tax Base

¹NR TWG 18-05 <https://www.local.gov.uk/topics/finance-and-business-rates/business-rates-retention>

statistics) could be reflected similarly to non-discretionary discounts and exemptions.

Q. Does the Group have any views on the best approach to factoring Local Council Tax Support in the fair funding review?

Council tax levels

18. As well as the size of tax bases, the amount of income which can be raised through council tax depends on the Band D level set by individual authorities. Once a measure of taxbase is agreed, the review will effectively multiply that by a council tax level which will result in the final value of the resources adjustment.
19. Past approaches to council tax income in LGFS methodologies have effectively scaled an assessment of relative sizes of tax base by a fixed 'notional' level which was applied to each authority.

'Actuals'

20. Recent funding methodologies relating to Core Spending Power have taken a different approach: Settlement Core Funding, used to calculate Revenue Support Grant allocations for the 2016-17 to 2019-20 multi-year settlement, includes a measure of an authority's Council Tax Requirement in 2015-16.
21. Furthermore, the distribution methodology for the Improved Better Care Fund considers the 'actual' amount of adult social care funding which can potentially be raised through the ASC Precept. Both of these methodologies therefore consider varying council tax levels as well as tax bases.
22. Such an 'actual' approach in a future needs and resources assessments would mean authorities which have higher Band D levels would receive proportionally less settlement funding than authorities with similar tax bases (and similar assessments of 'need') but lower Band D levels.
23. It would enable areas which do not raise as much income from council tax due to lower council tax levels to receive a larger proportion of settlement funding to meet their need.
24. However, by distributing less funding to areas due to their having higher council tax levels, this approach would be criticised for assuming that the amount of council tax paid by residents in England for the same level of public service should vary. It removes flexibility for the impact of local choice on what to charge residents for different levels of public service.

25. Furthermore, creating a link between local decisions and settlement allocations could cause undesired incentive effects.

'Notional'

26. A notional council tax level applied to each authority would mitigate these issues. There was consensus among the TWG for this approach due to the issues with 'actuals' discussed above among others. An example of a notional approach might be a flat level were applied to each authority, meaning those with similar tax bases and similar assessments of relative need will receive broadly the same amount of settlement funding, regardless of what they actually raise through council tax.

27. The trade-off of a flat notional level would be greater divergence in overall spending power, depending upon each authority's council tax level. The review will continue to explore the merits of a flat notional level as well as potential other 'notional' approaches to measuring council tax.

Q. Does the Group agree with the direction set out above for how to approach council tax levels in respect of a relative resources adjustment?

Particular factors

28. Specific factors which affect council tax were also discussed by the TWG, in recognition of which the review could create bespoke adjustments outside of a general approach. These included:

- Adult Social Care Precept
- Parishes
- Prevalence of certain types of Levying Bodies
- Past acceptance of the Council Tax Freeze Grant
- Other past circumstances

29. There was some consensus among the TWG that there was no need to adjust for these factors but they will continue to be considered.²

Q. Does the Group agree have any views with regard to the factors set out above?

Next steps

30. Subject to ongoing discussion with Ministers, the review intends to consult on possible high level approaches to resources in its next consultation exercise. This

² See publicly available minutes to November 2017 and March 2018: <https://www.local.gov.uk/topics/finance-and-business-rates/business-rates-retention>

will include questions relating to the above areas, as well as potentially other aspects of a council tax resources adjustment, such as how to measure council tax over a multi-year settlement period, and how to approach an adjustment for different tiers of authority.

Sales, Fees and Charges

31. The review has also considered whether to make an adjustment of authorities' relative abilities to raise income from sales, fees and charges (SFCs).³
32. SFCs are not currently taken into account in the assessment of local authority resources. They are, however, netted off from the variable used to proxy authority need – net revenue expenditure.
33. After considering analysis of the viability of making such a resources adjustment, and the arguments for and against, the review notes the following key points:
 - a. SFC income is generally **cost recovery or less**, so LAs are recovering money paid for service delivery;
 - b. It is **complex** and would therefore add further complexity to the FFR system, and be very difficult to predict the outcomes at local level;
 - c. it is **volatile** over time, making it difficult to measure;
 - d. it could lead to **undesired incentive effects**; and
 - e. **Parking surpluses** can be particularly high in certain areas and this could be considered further.
34. The review will consult on a preferred treatment of SFC income in due course.

Q. Does the Group have any views on how to factor SFC income in a resources adjustment?

³For a detailed summary the SFC landscape see NR 17-01 <https://www.local.gov.uk/topics/finance-and-business-rates/business-rates-retention>